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No. 379

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IN THE

Supreme Court of the United States

OCTOBER TERM 1943

JOE DEGNAN, *Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR FOR THE NINTH CIRCUIT and BRIEF IN SUPPORT OF PETITION

RAYMOND G. WRIGHT,
CLARENCE R. INNIS,
ARTHUR E. SIMON,
Counsel for Petitioner.

Office and P. O. Address:
1020 1411 Fourth Ave. Bldg.,
Seattle 1, Washington.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

TO THE HONORABLE THE SUPREME COURT OF THE UNITED STATES:

The petition of Joe Degnan respectfully shows to this Honorable Court:

A.

Summary Statement of the Matter Involved

This is a petition for a writ of certiorari to review and reverse a judgment of the United States Circuit Court of Appeals for the Ninth Circuit for error in affirming a decision of the United States Board of Tax Appeals (now The Tax Court of the United States).

On September 22, 1941, your petitioner filed with the United States Board of Tax Appeals his petition for a redetermination of a deficiency of petitioner's income tax for the taxable year 1939 (R. 3) as as-

sessed in the notice of deficiency mailed to petitioner by the Commissioner of Internal Revenue on June 26, 1941 (R. 8-12). The decision of the Tax Court of the United States sustaining the deficiency was entered November 2, 1942 (R. 31). A petition for review by the Circuit Court of Appeals for the Ninth Circuit was filed January 27, 1943 (R. 32-37). On June 29, 1943, that court rendered its opinion affirming The Tax Court of the United States and, upon the same day, its judgment was filed and entered (R. 57).

The deficiency in question resulted from the disallowance by the Commissioner of percentage depletion as claimed in the partnership return of a metal-mining partnership for the year 1939. His share of the income from the partnership was reported by petitioner in his individual return for 1939. Disallowance of this percentage depletion in the partnership return for the same year, raised the individual income of petitioner proportionately and produced the deficiency.

The basis for the disallowance by the Commissioner of the claimed percentage depletion was that income was first realized from the mining property in question during the year 1938 and that no election had been made in any *timely* return for that year to take percentage depletion and that under Section 114 (b) (4) of the Internal Revenue Code such percentage depletion could not be allowed in the absence of such election in a timely return for such year (R. 11).

Petitioner throughout this litigation has duly and consistently challenged the correctness of this interpretation of the statute both before the Board of Tax

Appeals (R. 4, 6) and before the Circuit Court of Appeals (R. 35).

The question involved is a pure question of law, concerned wholly with the meaning of the section of the statute. No issue of fact was before either of the lower tribunals, the matter having been submitted upon an agreed statement (R. 15-19) adopted by the Board of Tax Appeals (R. 23).

The metal mining partnership of which petitioner was a member duly filed its return for 1939 and therein by appropriate language claimed percentage depletion (R. 18, paragraph 8). Income had been first realized from the property during 1938 (R. 16, paragraph 3). No partnership return for 1938 was filed until September 18, 1940, at which time the return so filed contained appropriate language to elect to take percentage depletion (R. 17, paragraph 7).

The question is whether either of the said returns was a "first return" within the meaning of Section 114 (b) (4) which provides:

> "A taxpayer making his first return under this chapter * * * shall state whether he elects to have depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion * * *."[1]

Admittedly the section contains no reference to the time of filing the "first return" and contains no lan-

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[1]The complete text of the section is set forth in the Appendix following the Brief in support of this petition, *infra*, p. 1A.

guage restricting the election therein granted to a "timely" return. Yet The Board of Tax Appeals held that this was a requisite (R. 22) and the Circuit Court of Appeals affirmed (R. 57).

B.

Assignments of Error

1. The Circuit Court of Appeals erred in holding that the partnership return for 1939 was not a "first return" within the purview of the statute.

2. The Circuit Court of Appeals erred in holding that the partnership return for 1938 did not make an effective election entitling the taxpayer to the benefit of percentage depletion, because "not timely filed."

C.

Reasons Relied On for the Allowance of the Writ

1. The Circuit Court of Appeals has decided an important question of federal law which has not been, but should be, settled by this court.

It is manifest from both opinions below that the question here involved is one of first impression (R. 26, 50). That the construction of the section in question is important seems attested by the fact that this court has at least twice in recent years granted certiorari to pass upon its interpretation. *J. E. Riley Investment Co. v. Commissioner*, 311 U.S. 55; *Mother Lode Coalition Mines Co. v. Helvering*, 317 U.S. 222.

2. The decision, although one of first impression, is in conflict with *Ardbern Co. Ltd. v. Commissioner*, 120 F.(2d) 424, from the Fourth Circuit, and *Del*

Mar Addition v. Commissioner, 113 F.(2d) 410, from the Fifth Circuit, which hold, under analagous statutory provisions, that a return is to be given effect even though belated in filing.

3. The decision, we believe, misconceives the purport of the decisions of this court which it cites. It fails to recognize that in *Riley Investment Co. v. Commissioner*, 311 U.S. 55, and the other cases cited, this court was dealing with a problem essentially different from the instant one. In the *Riley* case, this court, we contend, set the limits upon the right to file amended, as distinguished from original, returns. The whole right to amend was non-statutory. *Haggar v. Helvering*, 308 U.S. 389. Setting the limits upon such a judicially accorded privilege is, we respectfully urge, a different problem than attempting, by judicial decision, to supply a time limit for action under a statute, wherefrom Congress, presumably advisedly, saw fit to omit such; and by decision, further, to add a cumulative, non-statutory penalty for tardiness in filing an original return, in addition to the penalties expressly set forth in the Revenue Code for belated filing. We urge, in this connection, that the decision fails to recognize the fundamental distinction between original and amended returns and fails to credit the writer of the opinion in the *Riley* case with accuracy in the use of language in the italicized portion of the following quotation:

> "Petitioner is seeking by this amendment not only to change the basis upon which its taxable income was computed for 1934 but to adopt a new method of computation for all subsequent years. That opportunity was afforded as a mat-

> ter of legislative grace; the election had to be made in the manner and in the time prescribed by Congress. The offer was liberal. But the method of its acceptance was restricted. *The offer permitted an election only in an original return or in a timely amendment.* An amendment for the purposes of §114 (b) (4) would be timely only if filed within the period provided by the statute for filing the original return. No other time limitation would have statutory sanction. To extend the time beyond the limits prescribed in the Act is a legislative not a judicial function." (311 U.S. 55, 59)

Also, we believe, the decision misses the injunction implicit in the last sentence of the quotation, that fixing time limits and penalties in addition to those in the Act, is not a proper judicial function.

Your petitioner presents herewith to this court, and files herewith as an exhibit hereto a duly certified transcript of the entire record in the case as the same appears in the United States Circuit Court of Appeals, together with your petitioner's brief in support of this petition.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Ninth Circuit, commanding that court to certify and send to this court for its review and determination, on a day certain to be therein designated, a full and complete transcript of the record and all proceedings of the said Circuit Court of Appeals in the case num-

bered and entitled on its docket, No. 10376, *Joe Degnan, Petitioner, v. Commissioner of Internal Revenue, Respondent*, and that the said judgment of the said Circuit Court of Appeals may be reversed by this Honorable Court and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

JOE DEGNAN,
Petitioner.

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CLARENCE R. INNIS,
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I.

OPINIONS OF THE COURTS BELOW

The Opinion of the Circuit Court of Appeals is reported in 136 F.(2d) 891, and in the record at pages 50 to 57. The Opinion of the Board of Tax Appeals is reported in 47 BTA 122 and appears in the record at pages 22 to 30.

II.

JURISDICTION

The date of the judgment to be reviewed is June 29, 1943 (R. 57).

Jurisdiction of this court to review the judgment of the Circuit Court of Appeals by the writ of certiorari is invoked under Judicial Code, §240, as amended by the Act of February 13, 1925, 43 Stat. 938; 28 U.S.C.A., §347.

III.

STATEMENT OF THE CASE

We are content to state the facts in the language of the Circuit Court of Appeals, as follows:

> "Petitioner Degnan and one Toivo J. Rosander entered into the partnership of Degnan and Rosander. The partnership acquired a metal mine in Alaska and derived the first items of deductible expense with respect to the property subsequent to the date of acquisition, May 12, 1938.
>
> "Pursuant to an agreement of the partners the net income of the partnership for 1938 was distributed to Degnan. He filed a timely individual income tax return for the calendar year 1938, reporting all income from and claiming deductions relating to the metal mine. No deduction for depletion was included. The other partner, Rosander, also filed a timely individual return for 1938, showing no income and no deduction with reference to the mining property.
>
> "Although no request for an extension of time to file had been made or granted, a 1938 return for the partnership was not filed until September 18, 1940. Fifteen per cent of the gross income from the Alaskan mine, or $810.00, was one of the deductions claimed. The face of the return contained the statement: 'We elect to take depletion on basis of 15% of gross as provided by law.'
>
> "A timely partnership return for the year 1939 was filed on March 29, 1940. It too included a deduction of fifteen per cent of the reported gross income from the mine, or $5,110.30, and alleged: 'Election is hereby made to take depletion on the percentage basis as provided in

Section 114 (B) (4) Revenue Act of '32 and '34.' Neither partner in his individual return for 1939 included any item for depletion with respect to the property.

"The Commissioner determined a deficiency of $224.51 against the partnership for the year 1939 on the ground that no election permitting the computation of depletion on the percentage basis had been made pursuant to §114 (b) (4). The Board of Tax Appeals upon a stipulation of the facts reached an opinion in accord with that of the Commissioner. Degnan seeks reversal.

"The case involves the interpretation of applicable clauses of §114 (b) (4) of the Revenue Act of 1938, 26 U.S.C.A. Int. Rev. Code §114 (b) (4)[1], which permits a depletion allowance in the case of metal mines of fifteen per cent of the gross income from the property, requires a taxpayer to elect the percentage depletion method of computation in his 'first return * * * in respect of a property' and provides that in the absence of such an election the percentage method will not be considered. Whichever system of computation is first selected under the section will prevail in subsequent years. The depletion allowance constitutes a deduction in computing net income under §23 (m)." (R. 50 to 53)

IV.

SPECIFICATIONS OF ERROR

1. The Circuit Court of Appeals erred in holding that the partnership return for 1939 was not a "first return" within the purview of the statute.

2. The Circuit Court of Appeals erred in holding

that the partnership return for 1938 did not make an effective election entitling the taxpayer to the benefit of percentage depletion, because "not timely filed."

V.

ARGUMENT

In this case the partnership filed two returns in which it claimed an election to take percentage depletion, one for 1939 and one for 1938. If the return for the year 1939, which was the first return filed by the partnership, was a "first return" within the meaning of the statute, then the decision of the Circuit Court of Appeals is erroneous. This return was in all respects a proper return for the year in question and was filed in due time. The only basis upon which it was denied validity is that the regulations of the Treasury Department had purported to define "first return" as the return made for the first taxable year for which the taxpayer has any item of income or deduction with respect to such property. As we shall demonstrate under our first point below, it was not within the power of the Treasury Department by such a regulation to alter the plain meaning of the statute.

If this court should not agree with us upon this point, however, then it is our contention that the 1938 return was a proper medium in which the partnership might exercise the election accorded by the statute, and that the Circuit Court of Appeals erred in denying effect to this return for such purpose because it was tardily filed, it being our contention that the statute here under consideration did not make timeliness

of filing such return a condition of the right to make the election accorded by statute.

A.

The Partnership Return for 1939 Was a "First Return" Within the Purview of the Statute

At the outset we take it as axiomatic that if a statute is unambiguous and clear, and a literal interpretation does not lead to absurdity nor do violence to the purpose of the legislation as reflected by its legislative history, there is no room for construction, and the ordinary meaning of language should be allowed to prevail. *Helvering v. Hamel*, 311 U.S. 504, 510. By the same token departmental regulations are appropriate only where a statute is ambiguous or so general in its terms as to require interpretation. The Treasury Department cannot by regulation enlarge or modify the scope of a statute. 1 Mertens: Law of Federal Income Taxation, 87-89.

Accordingly, in the instant case, we deem it appropriate to point out that there is nothing in the legislative history of §114 (b) (4) which impels any departure from literal meaning. *Mother Lode Coalition Mines Co. v. Commissioner*, 317 U.S. 222, 226—footnote 4.

Also, if as that decision holds, "first return" means just what it says (p. 226) and not "first return made by a taxpayer having net income derived from a property," it would seem obvious that "first return" in the section may not properly be tortured into "the return made under that title for his first taxable year

(beginning after December 31, 1937) for which he has any item of income or deduction with respect to such property," as was attempted to be required by Article 23 (m)-5, Treasury Regulations 101, under the Revenue Act of 1938.[2]

The "first return" under §114 (b) (4) in the instant case was the partnership return of Degnan and Rosander for 1939 (R. 18, paragraph 8). Neither the Regulations of the Treasury Department nor the belated filing subsequently of a partnership return for 1938 (R. 17, paragraph 7) could properly deprive it of that status under the statute.

Nor does according their ordinary meaning to ordinary words in this situation lead to any absurdity. If a "first return" is held to mean just that, then an election expressed in the first return settles the issue. There is involved no question of recomputation of anything as in the case of amended returns, and the anxiety of the Circuit Court of Appeals regarding such complication stems from the failure of that Court to recognize that the instant case does not concern amended returns, or rights of amendment. This case involves original returns only and there was here, we submit, no proper occasion for discussion of the circumstances under which amendments may be allowed. Neither, in the instant case, was there any shifting or attempting to shift from one basis of depletion to another. The same election was expressed in both returns and there was no proper occasion to advert to

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[2]The full text of this article of the Regulations in question is set forth in the Appendix, *infra*, p. 3A.

confusion which would result if taxpayers were allowed to amend and shift. We have not asked that we be allowed to change any election we have made.

In this connection, further, while the partnership return for 1939—the "first return"—was "timely filed" (R. 18, paragraph 8), the holding of the Circuit Court of Appeals that it would cease to be so if tardily filed, seems strained and erroneous. We concede, of course, that Congress might have provided that a first return under this section should cease to be so unless filed by March 15th. But we submit that Congress can speak more plainly, and should be required to speak more plainly than has been done in any of the legislation now before the Court, to accomplish such a startling and momentous result. It will be recalled that the election provided for in the "first return" under this section governed not only the taxable year involved in the return itself, but all future years. If this Alaskan miner, Joe Degnan, is forever to be barred from claiming percentage depletion unless the critical partnership return is posted by midnight of March 15th, or within such extended period not exceeding six months as the Commissioner in the exercise of his uncontrolled discretion may upon application during such period allow, common fairness would seem to require that the law say so in terms which Joe Degnan can be shown. Yet the Circuit Court of Appeals says in the instant case:

> "It is true that both the section and the regulations are silent as to the time within which the 'first return' must be filed." (R. 54)

Not only that, but nowhere in the statute nor in the

regulations is there any intimation that tardiness in filing the return causes it to cease to be a return, or precludes the exercise of the statutory election therein.

Penalties for tardiness in filing, and for willful failure to file, are provided in detail by the Internal Revenue Code. Thus §291 provides an *ad valorem* penalty up to 25% for failure to file a timely return. §293 (b) adds another 50% if the delay is fraudulent. Finally §145 imposes the sanctions of the criminal law upon those whose failure to make a return is willful. Surely these statutory goads to action should allay the concern of the Circuit Court of Appeals about the possibility of a taxpayer postponing indefinitely filing his "first return" to his personal benefit and administrative confusion. If not, the remedy, we think, is for Congress and not for the courts by way of judicial legislation.

These statutory penalties, moreover, mark the distinction between the position of a taxpayer who files a belated original return and one who seeks belatedly to amend a timely original return. The former has presumably become liable to some penalty, the latter obviously has not. So there is no lack of logic in according them different treatment, a point which troubled the Board of Tax Appeals (R. 28). For this reason, likewise, the reasons cited by the Circuit Court of Appeals for imposing a time limit upon the judicially accorded privilege of amendment are not properly applicable to the instant problem, dealing, as it does, only with original returns and the meaning of the words of a statute.

So we say the statutory "first return" in the in-

stant case was the partnership return for the year 1939 and that the Regulations of the Treasury Department which would make a different return the "first return" in violation of the plain meaning of the statute are palpably erroneous and, in that far, void.

Legislative Approval of Regulations

The only attempted answer to this reasoning to be found in the opinion of the Circuit Court of Appeals is the suggestion that these regulations were the subject of legislative approval under the doctrine of the first *Reynolds* case (*Helvering v. Reynolds Tobacco Co.*, 306 U.S. 110).

The reply to this position is threefold:

(1) The doctrine that the absence of corrective legislation demonstrates legislative indorsement of regulations issued under prior law when the law is reenacted has never been deemed to apply where the law is plain and the regulation patently erroneous.

Louisville & N. R. Co. v. U. S., 282 U.S. 740;

U. S. v. Missouri Pac. Rd. Co., 278 U.S. 269, 280;

Iselin v. U. S., 270 U.S. 245;

U. S. v. Maryland Casualty Co. (C.C.A. 7) 49 F.(2d) 556;

Biddle v. Commissioner (C.C.A. 2) 86 F. (2d) 718, aff'd. 302 U.S. 573;

1 Paul & Mertens: Law of Federal Income Taxation, 52;

1 Mertens: Law of Federal Income Taxation, 88, 96.

(2) The doctrine of the first *Reynolds* case, even where the statute is ambiguous, is fallacious as applied to income tax regulations where the precise point involved is not shown to have been considered by Congress, and subsequent decisions of this court have either greatly restricted, or altogether overruled it.

Thus in *Helvering v. Hallock*, 309 U.S. 118, 121, it is said:

> "we walk on quicksand when we rty to find in the absence of corrective legislation, a controlling legal principle."

Mr. Mertens in his Law of Federal Income Taxation, p. 101, says of the present status of the first *Reynolds* case:

> "In *Helvering v. Reynolds* (313 U.S. 428), the United States Supreme Court substantially qualified, if it did not reverse, the general principle of statutory construction on which the decision in the prior *Reynolds* case was premised. It will be recalled that the Supreme Court in the earlier *Reynolds* case, which involved a sale of treasury stock, held that the regulations in effect over a long period of years, during which years the statute was frequently reenacted without change, acquired the force and effect of law. In the later *Reynolds* case the Court, without stopping to inquire whether prior interpretations as disclosed by administrative practice and rulings and lower federal court decisions were so uniform and consistent as to fall within the rule of Congressional adoption through re-enactment of the statute, declared that: 'That rule is no more than an aid in statutory construction.'

> "The later *Reynolds* case very clearly demonstrates the tenuous character of rules of statutory construction. The language of the various decisions in which the courts have appeared to place material reliance on the legislative history and other aids to construction as a matter of substance and merit should not be unduly relied upon. It is becoming increasingly apparent that on the whole these aids to construction are really no more or less than just that and that while they are useful at times in resolving statutory ambiguities they will be given the force and effect of law only under very limited and usual circumstances."

At page 97, Mr. Mertens refers to the doctrine of the first *Reyonlds* case, as applied to income tax legislation, as an anachronism in view of the complexity of income tax statutes and the frequency of their re-enactment. He says:

> "To suppose that Congress must correct each mistaken construction under the penalty of otherwise incorporating it into the fabric of the statute appears unwarranted."

The doctrine has been severely and properly criticised in texts and Law Review articles. Paul, Use and Abuse of Tax Regulations in Statutory Construction, 49 Yale L.J. 660, 663; Paul, Studies in Federal Taxation (3rd series) 426; Griswold, A Summary of the Regulations Problem, 54 Harvard L. R. 398, 400; Alvord, Treasury Regulations and the Wilshire Oil Case, 40 Columbia L.R. 252; Surrey, The Scope and Effect of Treasury Regulations under the Income, Estate and Gift Taxes, 88 U. of Penn. L.R. 556; Brown, Regulations, Re-enactment and The Revenue Acts, 54

Harvard L.R. 377; Feller, Addendum to the Regulations Problem, 54 Harvard L.R. 1311; Griswold, Postscriptum, 54 Harvard L. R. 1323.

We submit that there is not strength enough left in the doctrine of the first *Reynolds* case to overcome the plain meaning of the statute and to justify denying to the 1939 return its manifest status as the "first return."

(3) Finally, if the doctrine of legislative approval has any potency, what of legislative disapproval? It is to be recalled that in the instant situation, the requirement of election which was provided by §114 (b) (4) has now been eliminated from the section by §145 (a) of the Revenue Act of 1942—Public Law No. 753, 77th Congress, 2nd Sess. If re-enactment spells approval, should not repeal indicate disapproval? If the former gives potency, should not the latter altogether abolish?

In conclusion, therefore, on this point we believe we have demonstrated that the 1939 return was the "first return" under the statute; that it was in all respects proper, and that the election therein properly set forth should have been given effect.

If we be mistaken, however, in the foregoing position, and the Circuit Court of Appeals should be right in holding that our subsequently filed 1938 partnership return was the "first return" specified in the statute by reason of the Regulations, still our election therein set forth would have been proper and should have been, and should now be, treated as effective. The only consideration to the contrary is the sug-

gestion that this return was not "timely." Our answer is that nothing in the statute and nothing, for that matter, in the regulations imposes any such requirement upon an original return for this purpose.

B.

The Decision of the Circuit Court of Appeals Erred In Holding That Timely Filing Is a Requisite for An Election to Take Percentage Depletion In An Original Return

As above pointed out, §114 (b) (4) contains no requirement as to the time of filing returns. There is no specific reference, either in the body of the section or in its title, to the time element. The section requires only that the election be made in "*first* return under this chapter in respect of a property."

Penalties for lateness in filing are provided by other sections of the law. The Internal Revenue Code in §291 provides an *ad valorem* penalty up to 25% for failure to file a timely return. §293 (b) adds another 50% if the delay is fraudulent. Finally §145 imposes the sanctions of the criminal law upon those whose failure to make a return is willful. If these provisions are not severe enough, the remedy we think, is for Congress, not for courts by judicial legislation. An additional and more burdensome penalty should not be read into the statute by implication. We respectfully submit that a duplication of penalties is not to be implied or assumed in the absence of clear and compelling language.

As the opinion of the Board of Tax Appeals herein

points out, "there appear to be no cases directly in point" on the construction of this section of the statute with reference to any requirement of the time of filing the return (R. 26).

In *Ardbern Co., Ltd. v. Commissioner of Internal Revenue*, 120 F.(2d) 424, however, the Circuit Court of Appeals for the Fourth Circuit decided an issue substantially similar to the instant one in accord with the proposition for which we here contend. The Court had before it in that case the construction of a statute concerning foreign personal holding corporations. Under the provisions of Section 233 of the Revenue Acts of 1928 and 1932 such corporations could receive the benefit of deductions and credits "only by filing or causing to be filed with the Collector a true and accurate return of total income from all sources in the United States prescribed" in the Act. In that case the taxpayer failed to file such an income tax return with the Collector until after the deficiency notice had been given. The Commissioner there, as here, contended that such a belated return could not be given any effect, relying strongly upon the case of *J. E. Riley Investment Co. v. Commissioner*, 311 U.S. 55, 61 S. Ct. 95, 85 L. ed. 36. The Court overruled the contention of the Commissioner upon the ground we here urge, in the following language:

> "While there is a specific penalty of 25 per centum fixed for failure to file tax returns, Section 291, Revenue Act of 1928, 26 U.S.C.A. Int. Rev. Acts, page 431, there is no provision that there shall be an added penalty in the form of not allowing the delinquent taxpayer deductions to which it otherwise would be entitled."

The Court distinguished the *Riley* case upon the ground that the latter case dealt with an amended return whereas in the *Ardbern* case, as here, the taxpayer's claim was based upon his "first" return.

Similarly, the Circuit Court of Appeals for the Fifth Circuit, in *Del Mar Addition v. Commissioner*, 113 F.(2d) 410, held that a delinquent capital-stock tax return, although filed only five days before the date set for hearing on deficiencies was to be given effect. In that case, the specific sections of the statute made no provision for the filing of delinquent returns. The court held, however, that since the general statute provided a penalty for delinquency, as in the case of §291 here, there was a necessarily implied right to file a delinquent return and that a "first return" under the statute there under consideration, did not cease to be such because not timely filed.

These cases from the Fourth and Fifth Circuits are, we submit, opposed to the holding in the instant case. Although cited to the court, they are not mentioned in the opinion. Certiorari should be granted to resolve the conflict in a situation which has not been passed upon by this Court.

The decision of the Circuit Court of Appeals herein quotes largely from the case of *Riley v. Commissioner*, 311 U.S. 55, and three other recent cases from this Court involving amended returns. These cases established the right of a taxpayer to make amendments—a non-statutory matter. Also, in the light of the administrative difficulties attendant upon an unlimited right to amend, these cases established a limit upon

such right. To us it seems clear that these cases are not in point here and the difficulties to which they advert are not present in our situation involving, as it does, only original returns and no attempted shifting. The language of those cases is to be considered in the light of the problems there before the court. Because in the *Riley* case, this court held that an amended return could not be filed after the delinquent date, it does not at all follow that an *original* return cannot properly be so filed. As above pointed out, there is no statutory penalty which would deter delinquency in making amendments of returns. There are specific statutory penalties which apply to tardiness in filing original returns. We believe these latter should here be held the exclusive penalties and that additional ones should not be supplied by judicial fiat.

The distinction between original and amended returns which seems to have escaped the Circuit Court of Appeals is well illustrated in *Jordan Creek Placers v. Commissioner*, 43 B.T.A. 131, 137, where it was held that a belated "first return" fixing capital stock tax status was to be given effect although recognizing that if there had been a prior return it would have been too late to amend under the doctrine of the *Riley* case.

To us it seems that the section in question presents no ambiguity. There is really no occasion for construction in the technical sense. If there were, however, we fail to find any empirical evidence from the legislative history of this section, as distinguished from juristic speculation, that literal interpretation defeats its purpose. With reference to supposed ad-

ministrative expediency, it is perhaps in order to recall that the requirement of election was first made a part of the Revenue Law in 1932 (Cf. *Tonopah Mining Co. v. Commissioner* (C.C.A. 3) 127 F.(2d) 239, 240). It is also proper to notice that it has been removed by the Revenue Act of 1942. As the fourth footnote to the decision in *Mother Lode Coalition Mines Co. v. Helvering*, 317 U.S. 222, 226, points out, nothing in the legislative history of the provision casts any light on its purpose.

Accordingly we respectfully contend that the Circuit Court of Appeals erred in attempting to add timeliness of filing to the requirements of §114 (b) (4).

VI.

CONCLUSION

It is, therefore, respectfully submitted that this case is one calling for the exercise by this Court of its supervisory powers and that a writ of certiorari should be granted to review and reverse the decision of the Circuit Court of Appeals herein.

RAYMOND G. WRIGHT,
CLARENCE R. INNIS,
ARTHUR E. SIMON,
Counsel for Petitioner.

Office and P. O. Address:
1020 1411 Fourth Ave. Bldg.,
Seattle 1, Washington.

APPENDIX

Revenue Act of 1938, c. 289, 42 Stat. 447:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * * * *

(m) *Depletion.*—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary.

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(b) *Basis for Depletion.*—

(1) *General rule.*—The basis upon which depletion is to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determinating the gain upon the sale or other disposition of such property, except as provided in paragraphs (2), (3), and (4) of this subsection.

* * * * * * * *

(4) *Percentage depletion for coal and metal mines and sulphur.*—The allowance for depletion under section 23 (m) shall be, * * * in the case of metal mines, 15 per centum, * * * of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect to the prop-

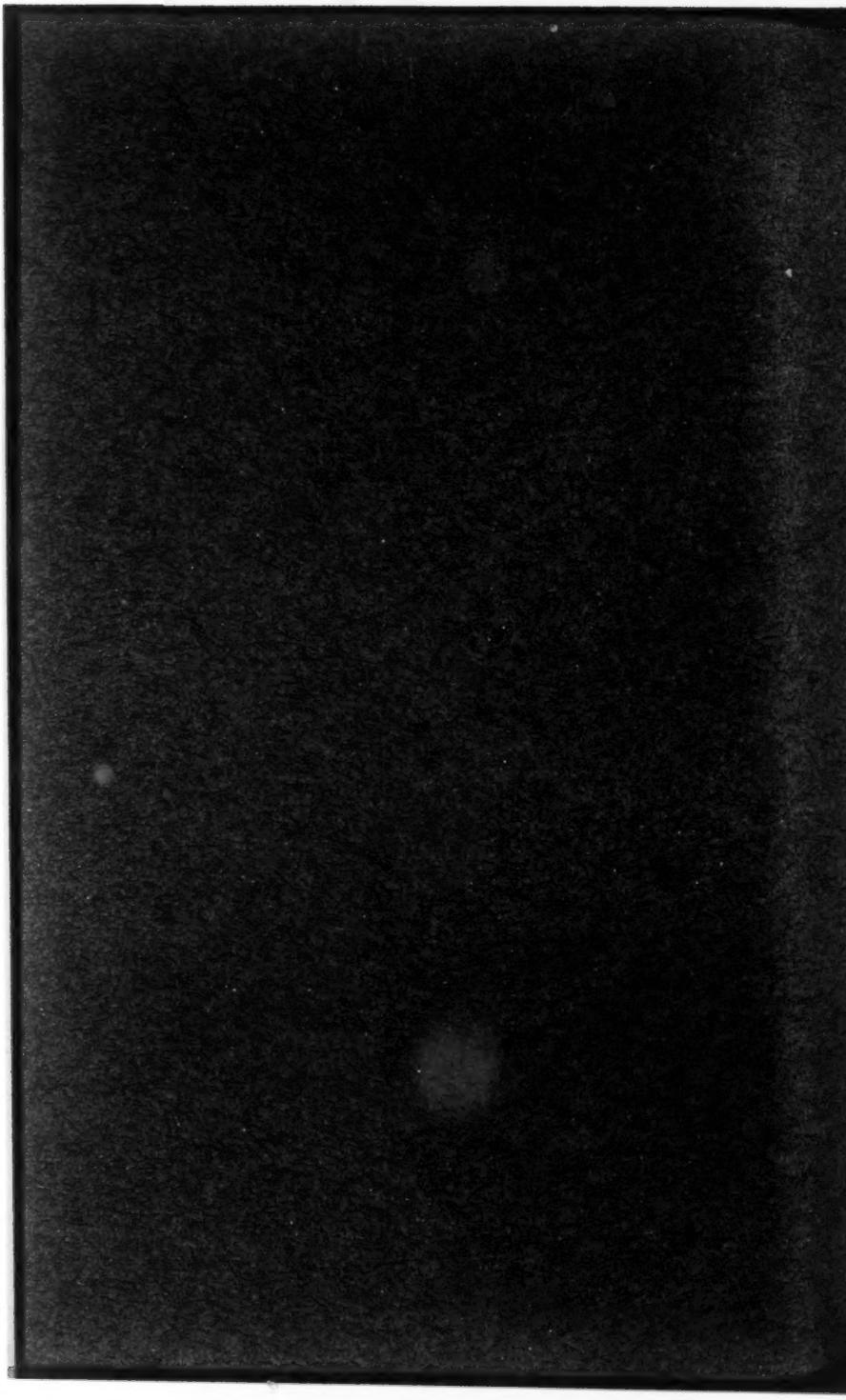
erty. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property. A taxpayer making his first return under this title in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion, and the depletion allowance in respect of such property for such year shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for such year shall be computed without reference to percentage depletion. The method, determined as above, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either directly or through one or more substituted bases, as defined in that section. The above right of election shall be subject to the qualification that this paragraph shall, for the purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuation of section 114 (b) (4) of the Revenue Act of 1934 and the Revenue Act of 1936, and as giving no new election in cases where either of such sections would, if applied, give no new election.

Treasury Regulations 101, promulgated under the Revenue Act of 1938:

ART. 23 (m)-5.—*Computation of depletion based on a percentage of income in the case of coal mines, metal mines, and sulphur mines or deposits.*—Under section 114 (b) (4) a taxpayer may deduct for depletion an amount equal to 5 per cent of the gross income from the property during the taxable year in the case of coal mines, an amount equal to 15 per cent of the gross income from the property during the taxpable year in the case of metal mines, and an amount equal to 23 per cent of the gross income from the property during the taxable year in the case of sulphur mines or deposits, but such deduction shall not in any case exceed 50 per cent of the net income of the taxpayer (computed without allowance for depletion) from the property. (For definitions of "gross income from the property" and "net income of the taxpayer (computed without allowance for depletion) from the property," see article 23 (m)-1 (g) and (h).)

Subject to the qualifications specified in the last sentence of this paragraph, a taxpayer making his first return under Title I of the Act (for a taxable year beginning after December 31, 1937) in respect of a property must state as to each such property whether he elects to have the depletion allowance for each such property for the taxable year computed with or without reference to percentage depletion. For the purpose of this article the taxpayer's first return under Title I of the Act in respect of a property is the return made under that title for his first taxable year (beginning after December 31, 1937) for which he has any item of income or deduction

with respect to such property. An election once exercised under section 114 (b) (4) and this article cannot thereafter be changed by the taxpayer, and the depletion allowance in respect of each such property will for all succeeding taxable years be computed in accordance with the election so made. If the taxpayer fails to make such statement in the return in which the election should be so indicated, the depletion allowance for the year for which an election must be first exercised and for all succeeding taxable years will be computed without reference to percentage depletion. The method, determined under section 114 (b) (4) and this article, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer either directly or through one or more substituted bases, as defined in that section. The right of election specified in this paragraph is subject to the qualification that section 114 (b) (4) shall, for the purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuation of section 114 (b) (4) of the Revenue Act of 1934 and the Revenue Act of 1936, and as giving no new election in cases where either of such sections would, if applied, give no new election.



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554847—43

In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 379

JOE DEGNAN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 23–30) is reported at 47 B. T. A. 122. The opinion of the Circuit Court of Appeals (R. 50–57) is reported at 136 F. 2d 891.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 29, 1943 (R. 57). Petition for a writ of certiorari was filed September 24, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether an election to compute depletion on a percentage depletion basis is made in a "first return" as required by Section 114 (b) (4) of the Internal Revenue Code, either when stated in a delinquent return for the year in which income was originally derived from the property or in a timely-filed return for the subsequent year.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. 7–12.

STATEMENT

Petitioner was an equal partner in a partnership known as Degnan and Rosander (R. 23). On or about May 12, 1938, the partnership acquired a metal mine near Ophir, Alaska. The first items of income from the property were derived and the first items of deductible expenses were incurred by the partnership during the calendar year 1938 subsequent to May 12. (R. 23–24.)

All of the net income of the partnership for 1938 was distributed to the petitioner pursuant to an agreement between the partners. Petitioner reported all items of income derived from the property during 1938 in his individual return for that year. He claimed deductions in respect of the property and a net income therefrom was

included in his taxable income. He did not claim any deduction for depletion in respect of the property. Rosander did not report any part of the income realized from the property in his return for 1938, nor did he claim any deduction in respect of the property for that year. (R. 24.)

The partnership did not file a return for the year 1938 until September 18, 1940, when a return was made to the Collector of Internal Revenue at Tacoma, Washington. The return disclosed gross income of $5,400 and total deductions of $2,571. The deductions included the amount of $810 representing depletion computed on a percentage basis (R. 24). The following notation appeared on the face of the return (R. 24–25):

> We elect to take depletion on the basis of 15% of gross as provided by law.

No request had been made by or on behalf of the partnership for an extension of time within which to file its return for the year 1938, and no extension was granted (R. 25).

The partnership filed a timely return for the year 1939 on March 29, 1940. Included among the deductions reported on that return was the amount of $5,110.30 representing depletion claimed on the percentage basis. The following notation appeared on that return (R. 25):

> Election is hereby made to take depletion on the percentage basis as provided in

section 114 (B) (4) Revenue Act of '32 and '34.

In determining a deficiency against the petitioner for the tax year 1939, the Commissioner disallowed the depletion allowance claimed in the partnership return, on the ground that the election to take percentage depletion, required by Section 114 (b) (4) of the Internal Revenue Code, had not been made in a timely return filed for the year 1938 when income from this property was first realized; a smaller deduction was allowed computed on the basis of cost, thus increasing the petitioner's net income from the partnership (R. 10–11). The Board of Tax Appeals sustained the Commissioner (R. 30) and the decision was affirmed by the court below (R. 57).[1]

ARGUMENT

The court below correctly decided this case in accordance with the decisions of this Court in *Mother Lode Co.* v. *Helvering,* 317 U. S. 222, and *Riley Co.* v. *Commissioner,* 311 U. S. 55. Under the statute (Appendix, *infra*) a taxpayer cannot take percentage depletion unless he has made an express election in his "first return * * * in re-

[1] The same issue arose in determining a deficiency against the other partner, Rosander. The two cases were consolidated for consideration and decision before the Board of Tax Appeals (R. 21–22). Upon order of the Circuit Court of Appeals, the Rosander proceedings were suspended to await final decision in the instant case (R. 38–39).

spect of a property."[2] The *Mother Lode* case approved the regulations (Appendix, *infra*) which define the term "first return" to mean the return made for the first taxable year for which there is any item of income or deduction with respect to the property. Thus it is clear that the election indicated in the 1939 partnership return was ineffectual.

The *Riley* case, holding that an election cannot be made in an untimely amendment to a return, makes it equally plain that the partnership could not make an effective election in an untimely return filed for 1938. If a taxpayer were permitted to make his election in an untimely original return, he would have the same advantages of hindsight which, under the *Riley* case, he could not obtain through use of an untimely amendment. The Government would also be confronted with the same difficulties of administration.[3]

There is no conflict among the circuits. Neither *Ardbern Co.* v. *Commissioner,* 120 F. 2d 424

[2] The entire problem is moot with respect to tax years beginning after December 31, 1941. Under Section 145 of the Revenue Act of 1942, c. 619, 56 Stat. 798, depletion deduction may thenceforth be computed either on cost or percentage basis without regard to election.

[3] Although the partnership return for 1938 was the appropriate vehicle for stating the election, it may be urged that under the peculiar facts of this case the partnership was already precluded from taking percentage depletion by petitioner's failure to indicate an election in his individual return for 1938 in which he reported all income and deductions from the partnership property.

(C. C. A. 4th), nor *Del Mar Addition* v. *Commissioner,* 113 F. 2d 410 (C. C. A. 5th), the cases upon which petitioner relies, were concerned with the statute which is involved in the instant case. Both of those cases permitted untimely returns to be effective under different statutes upon considerations of equity, of which there are none present in the case at bar. Moreover, in view of this Court's later decision in *Scaife Co.* v. *Commissioner,* 314 U. S. 459, the *Del Mar Addition* case is probably no longer authoritative.

CONCLUSION

The petition for certiorari should be denied.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.
SAMUEL O. CLARK, Jr.,
Assistant Attorney General.
SEWALL KEY,
SAMUEL H. LEVY,
MARYHELEN WIGLE,
Special Assistants to the Attorney General.

OCTOBER 1943.

APPENDIX

Internal Revenue Code:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(m) *Depletion.*—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. * * * (26 U. S. C., Sec. 23.)

Section 23 (m) of the Revenue Act of 1938, c. 289, 52 Stat. 447, is identical.

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

* * * * *

(b) *Basis for Depletion.*—

(1) *General rule.*—The basis upon which depletion is to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain upon the sale or other disposition of such property, except as provided in paragraphs (2), (3), and (4) of this subsection.

* * * * *

(4) *Percentage depletion for coal and metal mines and sulphur.*—The allowance

for depletion under section 23 (m) shall be, * * * in the case of metal mines, 15 per centum, * * * of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property. A taxpayer making his first return under this chapter in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion, and the depletion allowance in respect of such property for such year shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for such year shall be computed without reference to percentage depletion. The method, determined as above, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either directly or through one or more substituted bases, as defined in that section. The above right of election shall be subject to the qualification that this paragraph shall, for the purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuation of section 114 (b)

(4) of the Revenue Act of 1934, 48 Stat. 710, and the Revenue Act of 1936, 49 Stat. 1686, and the Revenue Act of 1938, 52 Stat. 494, and as giving no new election in cases where either of such sections would, if applied, give no new election. (26 U. S. C., Sec. 114.)

Section 114 (b) (1) and (4) of the Revenue Act of 1938 is substantially the same.

SEC. 53. TIME AND PLACE FOR FILING RETURNS.

(a) *Time for Filing.*—

(1) *General rule.*—Returns made on the basis of the calendar year shall be made on or before the 15th day of March following the close of the calendar year. Returns made on the basis of a fiscal year shall be made on or before the 15th day of the third month following the close of the fiscal year.

(2) *Extension of time.*—The Commissioner may grant a reasonable extension of time for filing returns, under such rules and regulations as he shall prescribe with the approval of the Secretary. Except in the case of taxpayers who are abroad, no such extension shall be for more than six months.

* * * * *

(26 U. S. C., Sec. 53.)

Section 53 (a) (1) and (2) of the Revenue Act of 1938 is identical.

SEC. 187. PARTNERSHIP RETURNS.

Every partnership shall make a return for each taxable year, stating specifically the items of its gross income and the deductions allowed by this chapter and such other information for the purpose of car-

> rying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe, and shall include in the return the names and addresses of the individuals who would be entitled to share in the net income if distributed and the amount of the distributive share of each individual. The return shall be sworn to by any one of the partners. (26 U. S. C., Sec. 187.)

Section 187 of the Revenue Act of 1938 is identical.

Treasury Regulations 103, promulgated under the Internal Revenue Code:

> SEC. 19.23(m)-5.—*Computation of depletion based on a percentage of income in the case of coal mines, metal mines, and sulphur mines or deposits.*—Under section 114 (b) (4) a taxpayer may deduct for depletion an amount equal to 5 percent of the gross income from the property during the taxable year in the case of coal mines, an amount equal to 15 percent of the gross income from the property during the taxable year in the case of metal mines, and an amount equal to 23 percent of the gross income from the property during the taxable year in the case of sulphur mines or deposits, but such deduction shall not in any case exceed 50 percent of the net income of the taxpayer (computed without allowance for depletion) from the property. (For definitions of "gross income from the property" and "net income of the taxpayer (computed without allowance for depletion) from the property," see section 19.23(m)-1 (*f*) and (*g*).)

Subject to the qualifications specified in the last sentence of this paragraph, a taxpayer making his first return under Chapter I (for a taxable year beginning after December 31, 1938) in respect of a property must state as to each such property whether he elects to have the depletion allowance for each such property for the taxable year computed with or without reference to percentage depletion. For the purpose of this section the taxpayer's first return under Chapter I in respect of a property is the return made under that chapter for his first taxable year (beginning after December 31, 1938) for which he has any item of income or deduction with respect to such property. An election once exercised under section 114 (b) (4) and this section cannot thereafter be changed by the taxpayer, and the depletion allowance in respect of each such property will for all succeeding taxable years be computed in accordance with the election so made. If the taxpayer fails to make such statement in the return in which the election should be so indicated, the depletion allowance for the year for which an election must be first exercised and for all succeeding taxable years will be computed without reference to percentage depletion. The method, determined under section 114 (b) (4) and this section, of computing the depletion allowance shall be applied in the case of the property for all taxable years in which it is in the hands of such taxpayer, or of any other person if the basis of the property (for determining gain) in his hands is, under section 113, determined by reference to the basis in the hands of such taxpayer, either di-

rectly or through one or more substituted bases, as defined in that section. The right of election specified in this paragraph is subject to the qualification that section 114 (b) (4) shall, for the purpose of determining whether the method of computing the depletion allowance follows the property, be considered a continuation of section 114 (b) (4) of the Revenue Act of 1934 and the Revenue Act of 1936, and the Revenue Act of 1938, and as giving no new election in cases where any of such sections would, if applied, give no new election.

Article 23 (m)–5 of Treasury Regulations 101, promulgated under the Revenue Act of 1938, is identical with the above except that in the second paragraph the beginning date is December 31, 1937, and the words "under chapter 1" appear of "under Title I of the Act."

U. S. GOVERNMENT PRINTING OFFICE: 1940